

**STATE OF ILLINOIS**

**ILLINOIS COMMERCE COMMISSION**

<b>Gallatin River Communications LLC</b>	:	
<b>d/b/a CenturyLink</b>	:	
	:	
<b>Petition for Arbitration Pursuant to</b>	:	<b>11-0567</b>
<b>Section 252(b) of the Communications</b>	:	
<b>Act of 1934, as amended by the</b>	:	
<b>Telecommunications Act of 1996 to</b>	:	
<b>Establish the Rates, Terms and</b>	:	
<b>Conditions of Interconnection with</b>	:	
<b>NTS Services Corp.</b>	:	

**PROPOSED ARBITRATION DECISION**

DATED: June 14, 2012



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**PROPOSED ARBITRATION DECISION**

By the Commission:

**I. PROCEDURAL BACKGROUND**

This proceeding was initiated pursuant to a Petition (hereinafter, the "Arbitration Petition") for Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 ("1996 Act"), 47 U.S.C. § 252 (b), to Establish an Interconnection Agreement ("ICA") with NTS Services Corp. ("NTS"), filed on August 3, 2011, by Gallatin River Communications L.L.C. d/b/a CenturyLink ("CenturyLink"). The Arbitration Petition identified two unresolved issues with respect to an attached "Interim" ICA, and detailed the position of each of the parties with respect to those issues. The Arbitration Petition indicated that the parties had failed to reach agreement on two rates, the pricing for (1) unbundled two wire loops and (2) unbundled DS-1 loops.

In support of its positions noted in the Arbitration Petition, on August 17, 2011, CenturyLink filed Direct Testimony. Pursuant to Notice, the Administrative Law Judge held a pre-hearing conference on August 22, 2011, in which the parties agreed to a schedule. Pursuant to the agreed to schedule, NTS filed a Response to the Arbitration Petition ("Response") along with Direct Testimony in support of its Response on September 23, 2011. In its Response, NTS also raised other issues for arbitration. On October 3, 2011, CenturyLink filed a Motion to Strike the additional issues raised by NTS. On November 7, 2011, the Administrative Law Judge ("ALJ") granted a CenturyLink Motion to Strike the new issues NTS raised in its Response.

An Evidentiary Hearing was held on February 21, 2012, at the offices of the Illinois Commerce Commission (the "Commission") in Springfield, Illinois. Following hearing, the parties filed Initial and Reply Briefs. A Proposed Order was served on the parties.

## II. INTRODUCTION

The parties to this proceeding, CenturyLink and NTS, disagree as to the appropriate rates for two unbundled network elements (“UNEs”), the rates for unbundled two wire loops and for unbundled DS-1 loops. CenturyLink offers rates derived from a total element long run incremental cost study (“TELRIC”) it has submitted in this proceeding. NTS argues that the CenturyLink TELRIC study is not accurate and that CenturyLink’s offered UNE rates are unsupported. NTS compares CenturyLink’s proposed rates for the two UNEs at issue with prior rates and with rates in other similar density locations and proposes rates based on these comparisons.

## III. APPLICABLE STANDARDS

Section 252(d) of the 1996 Act addresses the pricing standards the Commission must follow. It provides in relevant part that:

(d) Pricing standards

(1) Interconnection and network element charges

Determinations by a State commission of the just and reasonable rate for the interconnection of facilities and equipment for purposes of subsection (c)(2) of section 251 of this title, and the just and reasonable rate for network elements for purposes of subsection (c)(3) of such section -

(A) shall be -

- (i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable), and
- (ii) nondiscriminatory, and

(B) may include a reasonable profit.

47 USC § 252(d)

To implement the directives of 1996 Act, the Federal Communications Commission’s (“FCC”) rules prescribe how UNE rates are to be established. Section 51.503(b) of the Federal Communications Rules state:

(b) An incumbent LEC’s rates for each element it offers shall comply with the rate structure rules set forth in §§ 51.507 and 51.509, and shall be established, at the election of the state commission—

- (1) Pursuant to the forward-looking economic cost-based pricing methodology set forth in §§ 51.505 and 51.511; or

(2) Consistent with the proxy ceilings and ranges set forth in § 51.513.

47 C.F.R. § 51.503(b)

In order to rely on proxy rates, the Commission must, as an initial matter, determine that it does not have cost information adequate to set rates based upon the FCC's prescribed forward-looking economic cost methodology. In particular, Section 51.513(a) states, in relevant part that:

(a) A state commission may determine that the cost information available to it with respect to one or more elements does not support the adoption of a rate or rates that are consistent with the requirements set forth in §§ 51.505 and 51.511. In that event, the state commission may establish a rate for an element that is consistent with the proxies specified in this section[.]

47 C.F.R. § 51.513(a)

Thus, as a threshold matter, the Commission must determine whether the cost information presented by CenturyLink in this proceeding is adequate to set rates based upon the FCC's prescribed forward-looking economic cost methodology.

The FCC's prescribed forward-looking economic cost methodology, TELRIC, is defined in Sections 51.505 and 51.511, of the FCC's TELRIC rules, and states:

§ 51.505 Forward-looking economic cost.

(a) In general. The forward-looking economic cost of an element equals the sum of:

(1) The total element long-run incremental cost of the element, as described in paragraph (b); and

(2) A reasonable allocation of forward-looking common costs, as described in paragraph (c).

(b) Total element long-run incremental cost. The total element long-run incremental cost of an element is the forward-looking cost over the long run of the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such element, calculated taking as a given the incumbent LEC's provision of other elements.

(1) Efficient network configuration. The total element long-run incremental cost of an element should be measured based on the use of the most efficient telecommunications technology currently

available and the lowest cost network configuration, given the existing location of the incumbent LEC's wire centers.

(2) Forward-looking cost of capital. The forward-looking cost of capital shall be used in calculating the total element long-run incremental cost of an element.

(3) Depreciation rates. The depreciation rates used in calculating forward-looking economic costs of elements shall be economic depreciation rates.

(c) Reasonable allocation of forward-looking common costs—

(1) Forward-looking common costs. Forward-looking common costs are economic costs efficiently incurred in providing a group of elements or services (which may include all elements or services provided by the incumbent LEC) that cannot be attributed directly to individual elements or services.

(2) Reasonable allocation.

(i) The sum of a reasonable allocation of forward-looking common costs and the total element long-run incremental cost of an element shall not exceed the standalone costs associated with the element. In this context, stand-alone costs are the total forward-looking costs, including corporate costs, that would be incurred to produce a given element if that element were provided by an efficient firm that produced nothing but the given element.

(ii) The sum of the allocation of forward-looking common costs for all elements and services shall equal the total forward-looking common costs, exclusive of retail costs, attributable to operating the incumbent LEC's total network, so as to provide all the elements and services offered.

(d) Factors that may not be considered. The following factors shall not be considered in a calculation of the forward-looking economic cost of an element:

(1) Embedded costs. Embedded costs are the costs that the incumbent LEC incurred in the past and that are recorded in the incumbent LEC's books of accounts;

(2) Retail costs. Retail costs include the costs of marketing, billing, collection, and other costs associated with offering retail telecommunications services to subscribers who are not telecommunications carriers, described in § 51.609;



(3) Opportunity costs. Opportunity costs include the revenues that the incumbent LEC would have received for the sale of telecommunications services, in the absence of competition from telecommunications carriers that purchase elements; and

(4) Revenues to subsidize other services. Revenues to subsidize other services include revenues associated with elements or telecommunications service offerings other than the element for which a rate is being established.

(e) Cost study requirements. An incumbent LEC must prove to the state commission that the rates for each element it offers do not exceed the forward-looking economic cost per unit of providing the element, using a cost study that complies with the methodology set forth in this section and § 51.511.

(1) A state commission may set a rate outside the proxy ranges or above the proxy ceilings described in § 51.513 only if that commission has given full and fair effect to the economic cost based pricing methodology described in this section and § 51.511 in a state proceeding that meets the requirements of paragraph (e)(2) of this section.

(2) Any state proceeding conducted pursuant to this section shall provide notice and an opportunity for comment to affected parties and shall result in the creation of a written factual record that is sufficient for purposes of review. The record of any state proceeding in which a state commission considers a cost study for purposes of establishing rates under this section shall include any such cost study.

#### 47 C.F.R. § 51.505

##### § 51.511 Forward-looking economic cost per unit.

(a) The forward-looking economic cost per unit of an element equals the forward-looking economic cost of the element, as defined in § 51.505, divided by a reasonable projection of the sum of the total number of units of the element that the incumbent LEC is likely to provide to requesting telecommunications carriers and the total number of units of the element that the incumbent LEC is likely to use in offering its own services, during a reasonable measuring period.

(b)(1) With respect to elements that an incumbent LEC offers on a flat-rate basis, the number of units is defined as the discrete number of elements (e.g., local loops or local switch ports) that the incumbent LEC uses or provides.

(2) With respect to elements that an incumbent LEC offers on a usage-sensitive basis, the number of units is defined as the unit of measurement of the usage (e.g., minutes of use or call-related database queries) of the element.

47 C.F.R. § 51.511

As the FCC has described its prescribed cost estimation methodology, “TELRIC equates the current market value of the existing network of an incumbent telecommunications provider with the cost the incumbent LEC would incur today if it built a local network that could provide all the services its current network provides, to meet reasonably foreseeable demand, using the least-cost, most efficient technology currently available.” See FCC, In the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers (“ILECs”), Implementation of the Local Competition Provisions of the 1996 Act, and Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket Nos. 01-338, 96-98, and 98-147, released August 21, 2003, at ¶ 670, (“First Report and Order”).

#### **IV. CONTESTED ISSUES**

The Commission notes that there appear to be only two contested issues present in this matter, those being what is the appropriate rate for unbundled 2-Wire Loops, and what is the appropriate rate for unbundled DS-1 Loops.

##### **A. CenturyLink Position**

CenturyLink suggests the Commission should adopt its proposed rates for 2-wire and DS-1 loops, arguing they are the only rates proposed that comply with the FCC’s regulations requiring the use of a properly prepared TELRIC study. CenturyLink asserts that none of the criticisms of the cost study presented by NTS or Staff justify rejection of CenturyLink’s cost study or the monthly recurring rates derived from the cost study. CenturyLink urges the Commission to reject the proxy rates proposed by NTS and Staff, asserting that the use of proxy rates is no longer authorized by federal law and because the proxies proposed by NTS and Staff are not reasonable in representing CenturyLink’s Illinois cost, nor based upon TELRIC.

CenturyLink notes the FCC’s regulations implementing the 1996 Act provide that UNE rates shall be based on the FCC’s prescribed forward-looking economic cost-based pricing methodology. Under this methodology, CenturyLink states the forward-looking economic cost of an element equals the sum of: (1) the total element long-run incremental cost of the element and (2) a reasonable allocation of forward-looking common costs. CenturyLink asserts the TELRIC of an element is the forward-looking cost over the long run of the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such an element. CenturyLink notes that TELRIC is measured based on the use of the most efficient

telecommunications technology currently available and the lowest cost network configuration, given the existing location of the ILEC wire centers.

In this case, to develop the TELRIC component of the forward-looking economic cost of 2-wire and DS-1 loops, CenturyLink's asserts its cost model determines the forward-looking, most efficient network architecture and calculates the forward-looking installed cost of UNE loops based on this architecture. CenturyLink avers the combined use of precise wire center locations and boundaries, geo-coded customer locations, actual road networks and terrain features allow CenturyLink's TELRIC model to design, engineer and construct the most efficient cable routes possible relative to these inputs and parameters. In addition, CenturyLink notes equipment items, such as Digital Loop Carriers ("DLC"), Cross Connects, cables and terminals, are designed and sized to a capacity to achieve efficiency to meet the total demand for services at the locations served by the equipment. In this way, CenturyLink claims its cost model satisfies the requirement that TELRIC be based upon the most efficient telecommunications technology currently available and the least cost network configuration given the existing locations of CenturyLink's wire centers.

When CenturyLink's cost study results are tested against the embedded (or existing) network, CenturyLink believes the many efficiencies reflected in the cost study become clear. Once the forward-looking installed cost is calculated, CenturyLink's cost model calculates capital and expense costs. CenturyLink notes the direct costs attributable to UNE loops consist of maintenance expenses and other direct network operations and support expenses. CenturyLink states that maintenance costs include such things as repairing damaged cable or maintaining digital circuit equipment, while other direct network operations and support expenses include such things as testing functions, circuit engineering and cable pair record maintenance. In accordance with the FCC's regulations, CenturyLink asserts its cost model uses a forward-looking cost of capital and forward-looking depreciation rates. CenturyLink states the efficiencies in the modeled expenses are demonstrated by a comparison with CenturyLink's actual costs.

CenturyLink states the rates calculated by its cost study also include a reasonable allocation of forward-looking common costs, which include such costs as accounting and information technology personnel, furniture, office equipment, general purpose computers and corporate operations. CenturyLink notes its cost study calculates a common cost factor using the current common costs in Illinois and dividing by Illinois TELRIC annual expenses, which factor is then applied back to the individual TELRIC annual expenses to allow for recovery of common costs in the monthly recurring 2-wire and DS-1 loop rates.

CenturyLink claims the reasonableness of the rates generated by its cost study is confirmed by other measures of reasonableness, noting the monthly recurring cost for loops in the Pekin exchange is in line with the range of rates approved in other states for comparable exchanges; while the reasonableness of the 2-wire rates is also confirmed when these rates are compared to the FCC's 1998 HCPM results. CenturyLink avers that the overall Band 1 rate is reasonable when compared to the

Band 1 rate for Verizon, which is the closest analog for CenturyLink in Illinois, and that this is particularly true when the Verizon Band 1 rate is indexed forward into current dollars.

CenturyLink claims that NTS' concerns with the rate study are unfounded, noting that for the most part, NTS merely questions the inputs to CenturyLink's cost model, and NTS did not propose alternative inputs to be used in the cost study to produce alternative rates. CenturyLink states that NTS did not challenge the design of CenturyLink's cost model.

While NTS witness Miri opines that the annual charge factors are higher than he has seen in other cost studies, CenturyLink avers that he does not state that they are incorrect for CenturyLink's rural service territory. CenturyLink suggests there was complete agreement by the parties at hearing that costs are higher in rural exchanges because rural exchanges have lower line densities than urban or suburban exchanges.

While Mr. Miri complains that certain costs do not belong in the cost study, such as a portion of CenturyLink's airplane costs, CenturyLink notes that the total expense attributed to airplanes in the cost study is only attributed to the Band 1 2-wire loop. CenturyLink asserts Mr. Miri does not dispute that the cost of airplanes is an example of a common cost that is properly allocated to the unbundled loop under the FCC's rules

Mr. Miri also questions how the underlying mechanisms for the model's investments in underground, aerial, feeder, drop, network interface device and DLC investments were chosen and how certain portions of the loop model were developed, however CenturyLink suggests there is no basis for Mr. Miri's concern as this information was provided by CenturyLink, and notes that CenturyLink's Exh. 2.1 describes the Loop Module in detail.

Although NTS speculates that the cost study may not handle poles owned by other utilities correctly, CenturyLink asserts the cost study reduces investment in poles to account for poles owned by electric utilities, noting that the maintenance cost for poles includes the costs that CenturyLink pays to use other utilities' poles, and maintenance cost is reduced by revenues received from other utilities for use of CenturyLink poles.

While NTS asserts that CenturyLink's proposed UNE Loop rates would be "catastrophic" for NTS, CenturyLink opines that this argument is neither a criticism of CenturyLink's cost study nor a legitimate basis for rejection of the cost study results under applicable law.

CenturyLink notes that Staff witness Zolnierrek takes issue with one aspect of CenturyLink's cost study, which is that the two wire loops included within CenturyLink's cost study model contains functionalities, and thus costs, that are not directly attributable to or reasonably incremental to such elements. CenturyLink suggests that Staff misinterprets an FCC statement that a TELRIC cost study must model a network built today "that could provide all the services its current network provides, to meet

reasonably foreseeable demand, using the least-cost, most efficient technology currently available.” CenturyLink notes that Staff contends that the use of a 12,000 foot copper/fiber breakpoint makes all of the loops it has modeled broadband capable., and that this higher bandwidth functionality which is included in the modeled configuration is not a functionality that is attributable or reasonably incremental to all of the two-wire loops that CenturyLink will be providing as UNEs. Thus, Staff asserts that it is inconsistent with TELRIC rules for CenturyLink to include the costs of broadband functionality in UNE rates that it will charge for loops that do not contain such functionality. CenturyLink notes the primary costs Staff focuses on are the cost of DLCs that are necessary at the copper/fiber breakpoint and the cost of fiber in the model.

CenturyLink suggests that Staff is incorrect for various reasons, including that the FCC has ruled that the 12,000 foot copper/fiber breakpoint is the proper design to be used in a TELRIC model.<sup>1</sup> CenturyLink argues the FCC’s determination on this point is binding on the Commission, and suggests that the Commission has recognized this by approving the 12,000 foot breakpoint in the two cases where the issue has previously been raised. In the first case, involving Illinois Bell Telephone, Docket No. 02-0864, CenturyLink notes the Commission determined that a 12,000 foot breakpoint was appropriate, but it allocated 25% of the common costs of DLCs to broadband rather than the UNE loop. In the second case, involving Verizon entities, Docket No. 00-0812, CenturyLink asserts the Commission approved rates agreed to as part of a settlement that were premised on the 12,000 foot breakpoint, however prior to the settlement, the Commission approved Verizon’s cost model with the 12,000 foot breakpoint design.

CenturyLink notes that Staff’s is arguing that CenturyLink’s model must not reflect a forward-looking design, and in essence, Staff is asserting that the model must be tied to the current capabilities of the existing network. According to Staff, if the existing network does not have 12,000 foot breakpoints between copper and fiber, the modeled network cannot use this design, however CenturyLink avers that the FCC’s rules clearly reject this view, noting that TELRIC assumes that the ILEC’s network is reconstructed using a forward-looking technology that would be used today if the network were built from scratch today. CenturyLink states the only attribute of the existing network that is to be included in a TELRIC cost study is the location of the incumbent LEC’s existing wire centers, and the network design to be used in a TELRIC cost study is not otherwise constrained by the attributes of the existing network. Furthermore, CenturyLink asserts that FCC Rule 51.503(c) provides that the rates an incumbent LEC charges shall not vary on the basis of “the type of services that the

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<sup>1</sup> First Report and Order, *In the Matter of implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, 11 FCC Rcd. 15499, ¶620 (Rel. Aug. 8, 1996)(“Local Competition Order”)(“New entrants should make their decisions whether to purchase unbundled elements or build their own facilities based on the relative economic costs of these options...In arbitrations of interconnection arrangements, or in rulemakings the results of which will be applied in arbitrations, states must set prices for interconnection and UNEs based on the forward looking, long-run, incremental cost methodology we describe below. Using this methodology, states may not set prices lower than the forward-looking incremental costs directly attributable to provision of a given element.)

requesting carrier purchasing such elements uses them to provide,” therefore the purpose for which UNEs may be used is not to be taken into consideration when modeling the network and deriving rates under a TELRIC standard, contrary to Staff’s assertion.

CenturyLink states that Staff’s position really only concerns the Band 2 and Band 3 rates, noting that the number of DLCs in the model for Band 1 is about equal to the number of DLCs in the embedded network for Band 1. However CenturyLink submits that if one were to use an 18,000 foot breakpoint instead of a 12,000 breakpoint, the monthly recurring cost of the Band 1 loop rate would decline by a small amount and that even if all of the DLCs were removed from the cost study, the decline would not be significant per loop. Thus, even if Staff’s argument complied with FCC rules, CenturyLink submits it would still not yield Staff’s proposed rate under the TELRIC standard.

CenturyLink notes it tested the allocation of 25% of the common DLC equipment to broadband, as the Commission directed be done in Docket 02-0864. CenturyLink asserts the impact to Band 1 2-wire loop cost was minimal, and as a result, the cost study does not include any of the costs of providing broadband in the cost of the 2-wire loop.

CenturyLink states that both Staff and NTS propose that the Commission set CenturyLink’s 2-wire and DS-1 loop rates equal to proxy rates derived from sources other than a TELRIC cost study for CenturyLink’s exchanges in Illinois. CenturyLink notes that Staff proposes that the rate for the Band 1 2-wire loop be the same rate Gallatin River negotiated with NTS prior to CenturyLink’s acquisition of the Gallatin River exchanges, while NTS proposes that the Commission set CenturyLink’s Band 1 2-wire rate nearly equal to the AT&T rate that applies in Bartonville, Illinois. CenturyLink states that NTS also proposes that the Commission set CenturyLink’s Band 1 DS-1 rate equal to the AT&T rate for Bartonville, Illinois.

CenturyLink asserts that both the NTS and Staff proxies are not appropriate, and suggest that NTS’ proposed use of AT&T proxies is unreasonable. CenturyLink notes that AT&T’s service territory is primarily urban and is on average about ten times as dense as CenturyLink’s service territory; moreover, CenturyLink argues that AT&T’s rates are skewed lower towards the higher density exchanges because of the large number of exchanges included in the calculation of AT&T’s UNE loop rates.

While Staff proposes using the \$17.93 rate negotiated in the 2006 Gallatin River ICA as a proxy, CenturyLink argues this proxy rate should be rejected because it is not based on a TELRIC cost study, as well as because it was negotiated six years ago, it does not represent a rate that reflects today’s costs.

CenturyLink notes that NTS and Staff also propose to use proxy rates to establish 2-wire and DS-1 loop rates, however CenturyLink asserts this is no longer permissible under federal law. CenturyLink states that Section 51.513 of the FCC’s initial regulations implementing the 1996 Act, the FCC did permit state commissions to

set UNE rates based on a TELRIC cost study or, in the absence of sufficient cost information, based on proxy rates prescribed by the FCC. However, CenturyLink avers that Section 51.513 was challenged on appeal and ultimately vacated by the Eighth Circuit Court of Appeals in *Iowa Utilities Board v. FCC*, 219 F.3d 744 (8th Cir. 2000). While portions of the Eighth Circuit decision were appealed to the United States Supreme Court, CenturyLink opines the portion of the Eighth Circuit decision vacating Section 51.513 was not appealed; therefore proxy rates are no longer permissible.

CenturyLink asserts that even when Section 51.513 was in effect, proxies could only be used in the absence of sufficient cost information, noting that under Section 51.513(b)(1) rates established based on proxies were to “be superseded once the state commission has completed review of a cost study that complies with the forward-looking economic cost based pricing methodology described in §§51.505 and 51.511, and has concluded that such study is a reasonable basis for establishing element rates.” In this case, CenturyLink submits it has presented a cost study that complies with the FCC’s pricing methodology as set forth in §§51.505 and 51.511, and that cost study remains a reasonable basis for establishing CenturyLink’s 2-wire and DS-1 rates even after considering the NTS and Staff criticisms of the cost study inputs and design. Given these facts, CenturyLink avers that the ordering of a proxy would not be defensible even had Section 51.513 not been vacated.

CenturyLink notes that Staff presented a single criticism of the cost study, in that it was not appropriate for the cost study to be based on a network design that uses a 12,000 foot breakpoint between copper and fiber. According to Staff, the 12,000 foot breakpoint makes the network modeled in CenturyLink’s cost study capable of providing more services than CenturyLink’s current network is capable of providing, however CenturyLink claims that the FCC has ruled that the 12,000 foot copper/fiber breakpoint is the proper design to be used in a TELRIC cost study. CenturyLink asserts the FCC’s determination on this point is binding on the Commission, just as it was upon CenturyLink for model criteria use, and as Staff itself recognized in its testimony, the Commission has approved the use of this design in two prior UNE proceedings in Illinois.

CenturyLink states that Staff’s bases its argument against the use of a 12,000 foot copper/fiber breakpoint, on a single clause in the FCC’s Triennial Review Order, which Staff Refers to as the First Report and Order. Staff cites paragraph 669 of the Triennial Review Order in which the FCC stated that “TELRIC equates the current market value of the existing network of an incumbent telecommunications provider with the cost the incumbent LEC would incur today if it built a local network that could provide all the services its current network provides, to meet reasonably foreseeable demand, using the least-cost, most-efficient technology currently available.” CenturyLink notes that Staff argues that this provision means that the network modeled in a TELRIC cost study cannot be capable of providing more or different services than the existing network provides.

CenturyLink suggests that Staff’s reliance upon this language from the Triennial Review Order is misplaced for various reasons. Including that this section prescribes a

minimum, not a maximum. CenturyLink notes the network modeled in a TELRIC study must be capable at a minimum of providing all of the services that the existing network provides, and suggest that this section in no way prohibits the modeled network from being capable of providing more services than the existing network provides

CenturyLink suggests that Staff's argument is really an argument that the modeled network must be based on the embedded or existing network, and if the existing network does not deploy DLCs at a copper/fiber breakpoint at 12,000 feet, the modeled network cannot do so either. CenturyLink asserts the FCC has clearly rejected this view, noting that in footnote 2020 of the Triennial Review Order, the FCC states that "it is appropriate for a TELRIC analysis to consider existing technology that is not currently deployed by an incumbent LEC..."

While Staff contends that the network modeled in the TELRIC cost study is capable of providing more services than CenturyLink's existing network can provide, CenturyLink notes the modeled network does not include the incremental electronics that are necessary to enable the provision of broadband, and it is the added electronics, not the 12,000 foot copper/fiber breakpoint, determines whether the loops are capable of providing broadband. CenturyLink opines that an 18,000 foot copper/fiber breakpoint could just as easily be used to provide broadband if the necessary electronics were added.

CenturyLink also contends that the majority of loops in the modeled network are within 12,000 feet of the wire center, and thus are broadband capable under Staff's reasoning, even without DLCs. CenturyLink asserts that the modeled DLCs are used as an aggregation point for an efficient cable network, not to provide broadband, and for Band 1, the number of DLCs in the existing network is very close to the number of DLCs in the modeled network. Because a majority of loop lengths are less than 12,000 feet, CenturyLink argues the use of a 12,000 foot copper/fiber breakpoint does not make its modeled network significantly more capable of providing broadband.

CenturyLink also claims that Staff's criticism of the 12,000 foot copper/fiber breakpoint design would amount to only a minor and easily changed input in the cost study, and suggests the Commission is authorized under federal law to order specific and supportable input changes in its determination. In prior generic proceedings to set UNE rates, CenturyLink states the Commission has approved a cost model in an initial phase of the proceeding and then ordered input changes be run in the approved model.

CenturyLink also claims that the use of proxies, as proposed by NTS and Staff for 2-Wire Loops, is not appropriate, noting that the FCC's current rules require state commissions to apply the TELRIC standard in setting UNE rates. CenturyLink states that the FCC has held that a state commission may not set prices lower than the forward-looking incremental costs directly attributable to provision of a given element. CenturyLink notes that in 2002, the FCC's determination requiring that UNE rates be priced at, and not below, TELRIC was upheld by the United States Supreme Court in *Verizon Communications, Inc. v. FCC*, 535 U.S. 467 (2002).



CenturyLink notes that NTS claims that state commission still retain the authority to set proxy rates, relying upon a California Public Utilities Commission ("CPUC") decision denying rehearing of an interconnection arbitration decision involving Covad Communications Company and Roseville Telephone Company, Docket 01-06-087, (June, 2001), ("the CPUC docket"). In its initial decision, CenturyLink opines the CPUC had used Pacific Bell UNE rates to set interim UNE rates for Roseville, subject to true-up with interest; however neither party had submitted a TELRIC cost study to support the rates being proposed. CenturyLink notes the CPUC indicated that its provision for a true up of the interim prices, with interest, assured Roseville that it would be appropriately compensated when its cost study was completed and final UNE prices were approved.

CenturyLink states that in the CPUC docket, Roseville, the ILEC, had submitted a cost analysis that did not even purport to be a TELRIC compliant cost study, as Roseville had taken the position that it would be too costly to prepare such a study. In lieu of a cost study, CenturyLink states Roseville developed a ratio between its embedded costs (including retail costs and rate of return) and Pacific Bell's embedded costs (including retail costs and rate of return), which it then multiplied this ratio times Pacific Bell's UNE rates to arrive at rates for Roseville's UNEs. CenturyLink asserts that in its decision, the CPUC determined that Roseville's methodology violated the FCC's prohibitions against the use of embedded costs, retail costs and rate-of-return; therefore it determined it could not use Roseville's ratio method to calculate UNE rates, even on an interim basis.

CenturyLink claims the 1996 Act specifically addresses the situation where neither carrier presents a TELRIC cost study, and provides that a state commission may resolve open issues in an interconnection arbitration "on the basis of the best information available to it from whatever source derived." CenturyLink complains that most of the cases cited by NTS in this issue are not on point.

While Staff also asserts that the Commission has authority to set proxy rates in lieu of TELRIC rates, CenturyLink also asserts that the dockets relied upon by Staff do not support its position. In *Southwestern Bell Tel. Co v. AT&T Communications*, 1998 U.S. Dist. LEXIS 15637 (W.D. Tx. 1998) cited by Staff, CenturyLink claims the Court merely held that it was permissible for a state commission to independently calculate a wholesale discount rate based on cost information provided to it, notwithstanding that the wholesale discount happened to fall with the FCC's prescribed proxy wholesale discount rates. CenturyLink asserts this docket did not involve an attempt by the Texas Commission to order a proxy rate without regard to the FCC's TELRIC rules.

In *Bell Atlantic-Delaware, Inc. v. McMahon*, 80 F. Supp. 218 (Del., 2000) the Court cited 47 U.S.C. §252(b)(4)(B) and noted that a state commission is entitled to rely upon the best evidence available to it in setting rates, however CenturyLink notes the use of proxy rates was not challenged by either party to the case and was therefore not at issue, therefore the Court did not hold that it was permissible to set a proxy rate that is not in any way based on TELRIC.

Staff also relies upon a Commission decision involving reciprocal compensation rates for a Hamilton County Telephone Co-Op and several other rural location exchange carriers ("RLECs"), Docket Nos. 05-0644 to 05-0648 and 06-0657 (Cons.). CenturyLink notes that in these dockets, the Commission determined that the Hatfield Associates, Inc. TELRIC cost model presented by the RLECs, when run with inputs determined by the Commission, was appropriate for setting reciprocal compensation rates for five of the six RLECs involved in the case, however, for LaHarpe Telephone Company ("LaHarpe"), the cost study produced an unusually high reciprocal compensation rate due to the unique nature of LaHarpe's network. CenturyLink notes that for LaHarpe, the Commission prescribed a reciprocal compensation rate equal to the average of the other five RLEC's TELRIC reciprocal compensation rates, therefore CenturyLink claims this docket does not stand for the proposition that the Commission can set a UNE rate proxy selected without regard to the FCC's TELRIC rules.

CenturyLink asserts that the FCC initially permitted the use of its prescribed proxy rates because the development of cost studies was in its infancy and because of the tight time frames imposed on interconnection arbitrations, however the instant proceeding comes before the Commission fourteen years after the 1996 Act became law, after the legality of the TELRIC standard has been fully litigated, and after the Telecommunications Industry has had time to develop and work with TELRIC cost models. CenturyLink notes the time frames in this arbitration were extended specifically to give both Staff and NTS time to evaluate CenturyLink's cost study and to propose alternative inputs should any be justified and legally supportable.

CenturyLink states that Staff's proxy rate for the 2-wire loop is not tied in any way to TELRIC, noting that Staff proposes that the Commission set CenturyLink's UNE rate equal to the \$17.93 rate negotiated by Gallatin River and NTS in 2006. CenturyLink avers that this rate was not the result of a TELRIC cost study and no party to this proceeding has claimed that it was, and as it was negotiated six years ago, it would not reflect today's costs even if it had been based on a TELRIC cost study at the time. While Mr. McClerren testified that he not aware of upward price pressure for retail telecommunications services, he admitted at hearing that he did not base his testimony on any analysis of costs of copper, fiber or other cost study inputs. Nor did he take into account the effect that line loss since 2006 has on per unit costs. Mr. McClerren stated on cross-examination that he based his testimony solely on retail tariff filings made with the Commission. Mr. McClerren further testified that he did not consider the impact of competition from cable and wireless providers which may have exerted downward price pressure on the tariffed retail rates.

In its initial brief, Staff evaluates the Verizon Band 1 2-wire loop rate established in 2006 but decided against recommending it ostensibly because Verizon's service territory is less dense than CenturyLink's service territory. According to Staff, CenturyLink's TELRIC Band 1 rate should be lower than Verizon's Band 1 rate because higher density equates with shorter loop lengths. CenturyLink states however, that density and loop length are separate factors. If a single customer resides in a square mile with an average loop length of 15,000 feet and a second customer line is added just adjacent to the first, the density doubles but the average loop length remains the

same. In contrast, if the second customer line is 5000 feet further from the Central Office but within the same mile, the density doubles and the average loop length actually increases to 17,500 feet  $((15,000+20,000)/2)$ . CenturyLink demonstrated the absence of a relationship between density and average loop length within its Band 1 wire centers.

CenturyLink notes that its proposed rate for Band 1 is lower than Verizon's Band 1 rate, when Verizon's rate is indexed forward to reflect today's costs. CenturyLink suggests that Verizon's Band 1 rate was set in 2006, and is based on cost data that is even older. When one indexes Verizon's rate forward to today's cost, the result is a Band 1 monthly recurring rate of approximately \$30.28 per loop. Thus, the Verizon Band 1 rate, when indexed forward to today's costs, demonstrates the reasonableness of CenturyLink's proposed 2-wire loop rate for Band 1.

CenturyLink recommends that the Commission find that the 2-wire and DS-1 rates produced by CenturyLink's cost study are just, reasonable and nondiscriminatory, and adopt the ICA and Price List presented with CenturyLink's Petition for Arbitration incorporating these rates.

## **B. NTS Position**

NTS suggests that CenturyLink has attempted to justify its proposed price increases through a cost study that is at best flawed, if not completely unreasonable. Due to the inadequacies and lack of reliability of the cost study, NTS notes that both it and Staff have suggested that a proxy rate should be used instead to determine reasonable UNE rates. While CenturyLink argues that the TELRIC study is reliable and that the Commission lacks authority to determine proxy rates, NTS believes that the TELRIC study can not be used and that instead, the Commission must use its statutory authority to determine reasonable proxy rates for CenturyLink's UNEs. As NTS argues that UNE rates historically have decreased over time, the most reasonable proxy would be slightly less than the UNE rates that were charged by CenturyLink's predecessors, Gallatin River Communications and Madison River Communications. At the highest end of the price range, NTS suggests the UNE rates approved by this Commission for the former Verizon exchanges in Illinois should be applied.

NTS notes that Section 251 of the 1996 Act grants state commissions the right, and the obligation, to approve ICAs between ILECs and competitive local exchange carriers ("CLECs"). 47 CFR §51.513 grants state commissions the authority to establish proxy rates when an approved TELRIC cost study is not available. State commissions have maintained, and continue to establish, the right to set proxy rates in ICAs.

During the evidentiary hearing, NTS notes that CenturyLink argued that this Commission does not maintain the authority to establish proxy rates in this proceeding. NTS states that the case cited by CenturyLink, *AT&T Corporation v. Iowa Utilities Board*, 525 U.S. 366 (1999), does not contain the word "proxy" anywhere in the thirty page decision. In fact, NTS suggests the case had nothing to do with state commission obligations, but instead focused on the FCC's authority to establish standards for ICAs:

In this case, we address whether the Federal Communications Commission has authority to implement certain pricing and nonpricing provisions of the Telecommunications Act of 1996, as well as whether the Commission's rules governing unbundled access and "pick and choose" negotiation are consistent with the statute.

NTS notes this case reached the Supreme Court in 1999 on appeal from the Eighth Circuit. The FCC also issued its first attempt to set a standard for UNE pricing six months after the 1996 Act went into effect. NTS states that almost immediately, ILECs and state commissions challenged the First Report and Order, with the cases ultimately being consolidated in the U.S. Court of Appeals for the Eighth Circuit, in *AT&T Corporation vs. Iowa Utilities Board*, 120 F. 3d 753 (1997).

NTS states that the Eighth Court of Appeals held that the FCC's First Report and Order overstepped its jurisdiction, interfering with the states' rights to determine interconnection rules. Specifically, the Court held that the TELRIC standard for setting UNE rates was invalid. In one of the now legendary quotes for telecommunications law, the Appeals Court held that the presumption of state authority was "hog tight, horse high, and bull strong, preventing the FCC from intruding on the states' intrastate turf." In effect, NTS argues the lower Court Circuit ruled in favor of the states' rights to set interconnection policies rather than the FCC, suggesting that it was solely a jurisdictional issue.

NTS notes the ILECs did not focus on jurisdiction; rather they challenged the network elements that must be made available in an ICA. NTS asserts the Court of Appeals held that the list established by the FCC was sufficiently reasonable to be granted deference as a decision by an expert administrative agency., and agreed with the ILECs that the ICA rights in the 1996 Act could not be read so broadly as to allow competitive carriers to "pick and choose" among different ICAs to create a single ICA.

This decision was appealed to the U.S. Supreme Court, where NTS avers the Supreme Court noted that the case presented primarily a jurisdictional argument, stating that:

This is, at bottom, a debate not about whether the States will be allowed to do their own thing, but about whether it will be the FCC or the federal courts that draw the lines to which they must hew.

NTS avers that the Supreme Court held that in regards to pricing authority under §252(c) of the 1996 Act, state commissions retained the right to establish rates, subject to FCC rules.

NTS opines that the challenge in the Eighth Circuit for proxy rates related to the FCC's proxy rates that state commissions should use if TELRIC costs were not available, specifically the state-specific rates contained in 47 CFR §51.513(c). NTS asserts the ILECs argued that the proxy rates did not accurately reflect their costs and

thus were artificially low, which was never appealed to the Supreme Court. In the decision on remand, NTS avers that the Eighth Circuit analyzed the proxy rules noting that they appeared to require states to use the FCC proxy prices until such time as prices consistent with TELRIC prices could be established. NTS states the Eight Circuit found this practice to be unreasonable, stating that:

The Supreme Court held that the FCC “has jurisdiction to design a pricing methodology.” AT & T Corp., 525 U.S. at 385. However, the FCC does not have jurisdiction to set the actual prices for the state commissions to use. Setting specific prices goes beyond the FCC's authority to design a pricing methodology and intrudes on the states' right to set the actual rates pursuant to 252(c)(2). Following the Supreme Court's opinion, we now agree with the FCC that its role is to resolve “general methodological issues,” and it is the state commission's role to exercise its discretion in establishing rates.

NTS argues that the Eight Circuit never addressed whether state commissions should use state commission developed proxy prices, absent information sufficient to establish a TELRIC rate. NTS suggests the vacated rule only applied to the imposition of the FCC proxy rates by state commissions.

Shortly after the 8th Circuit's remand decision, the CPUC faced the precise legal question raised by CenturyLink in an interconnection arbitration case where no approved TELRIC study existed. NTS asserts the CPUC found that it indeed continued to have the authority to set proxy rates:

At this time, neither party has yet proposed UNE prices that result from a compliant TELRIC study and that the Commission can approve as final prices. (D.01-02-042, at 3.) The Commission has initiated proceedings for setting final prices, and thus far Roseville has submitted an initial proposal for a TELRIC methodology.

In such circumstances, interim pricing is required. The FCC in fact expected the use of interim UNE prices when it promulgated regulations to implement the Telecom Act. At 47 CFR § 51.513(a), the FCC provided for the use of proxies if a state commission determines that it cannot rely on the information then available for adopting UNE prices in compliance with regulatory requirements. Given the deadlines for arbitration set forth in the Telecom Act, cost studies have not always been completed in time. Similarly, the courts have approved interim UNE pricing when cost studies are a subject of dispute and a statutory deadline must be met.

Although the use of proxies had been anticipated and approved, the specific proxy prices established in FCC regulations for interim use are not available to us. The U.S. Court of Appeals, Eighth Circuit, vacated the FCC proxies as rates that are properly within the discretion of State commissions to determine. (*Iowa Utilities Board II*, 219 F.3d, at 757.) The

court did not, however, find unlawful the establishment and use of proxies by State commissions.

Since this decision, NTS asserts that state commissions have routinely used proxy rates since the decision above to set UNE rates. For example, after the elimination of the unbundled network element platform, NTS notes state commissions set proxy rates to be in effect prior to the transition to market-based rates. NTS asserts that the Illinois Commerce Commission itself noted 47 CFR §51.513 in its decision regarding a recent ICA arbitration between AT&T and Big River Telephone Company<sup>10</sup> with no discussion as to whether the rule had been vacated.

NTS opines that CenturyLink, in its Initial Brief, fails to make any compelling arguments as to why the Commission should not rely on proxy rates, nor why the rates to be applied should diverge from those proposed by Commission Staff. Rather than continue with the same arguments made in NTS' Initial Brief, NTS would like to simply draw the Commission's attention to one issue that has not been fully addressed thus far.

NTS argues that the same logic that both NTS and Staff have used to develop suggested rates for DS-0 loops in the Pekin exchange, should also be extended to the rates to be charged in Band 2 and 3 exchanges. As Staff has noted, CenturyLink has brought no evidence to prove that its costs to provide services to any exchanges have increased. In fact, given that UNE prices have historically decreased, NTS argues no increases are warranted, and the prevailing rates should be maintained going forward for all exchanges.

NTS believes that the Commission continues to maintain authority to set proxy rates under the 1996 Act, and given the lack of an approved TELRIC cost study, the Commission should find that the rates previously applied by Madison River Communications and Gallatin River Communications are a reasonable proxy for all exchanges. At the outer price limit, NTS suggests the Commission consider the UNE rates set using an approved cost study for the former Verizon exchanges as a reasonable proxy for those that should be charged in CenturyLink's exchanges.

### **C. Staff Position**

With respect to two-wire loops, Staff argues the network modeled by CenturyLink in its TELRIC study is capable of providing more services than CenturyLink's current network is capable of providing and, therefore, is inconsistent with the FCC's TELRIC prescriptions. Staff opines that CenturyLink has modeled a network with the ubiquitous capability to provide higher bandwidth or broadband services, however, Staff notes CenturyLink's actual network does not contain such ubiquitous capability. In particular, while CenturyLink does not maintain a list of the number of loops in its existing network that do or do not meet the 12,000 feet engineering criteria, Staff suggests the number of DLCs included in the companies existing network are insufficient to provide the ubiquitous higher bandwidth or broadband services capability that is included in CenturyLink's cost model.

Staff states that including ubiquitous broadband capability increases costs above the costs of deploying a network designed to provide only voice grade telephone service. While CenturyLink suggests that modeling longer loop lengths does not result in significantly lower unit loop costs, Staff argues that moving from a 12,000 feet engineering criteria to an 18,000 feet engineering criteria can reduce costs significantly. Staff asserts the reduction is not insignificant, and may grossly understate the costs of modeling broadband capability that otherwise does not exist in CenturyLink's actual network.

While Staff agrees with CenturyLink witness Londerholm that broadband is not a functionality required by the FCC in defining the 2-wire loop element, Staff's position is that broadband capability is also not required by the FCC in defining the 2-wire loop element. In modeling such capability, where that capability does not exist, Staff suggests CenturyLink is modeling a local network that has the capability to provide services that its current network does not have the capability to provide, which increases two-wire loop costs above those that are consistent with TELRIC requirements. Staff argues the information submitted by CenturyLink is not an adequate basis upon which to set rates.

Staff notes that CenturyLink takes the position that the Commission cannot impose a proxy rate in this proceeding because the FCC rules providing for proxy rates were overturned. Specifically, CenturyLink witness Miller states:

Dr. Zolnierrek states in his testimony, [that] 47 CFR 51.513 appears to authorize the ability to assign proxy rates for UNEs. However, the Eighth Circuit Court of Appeals vacated Rule 51.513 in *Iowa Utilities Board v. FCC*, 219 F.3d 744 (8th Cir. 2000). This case was subsequently affirmed in part and reversed in part on other grounds by the U.S. Supreme Court in *Verizon Communications Inc. v. FCC*, 535 US 467 (2002). Because Rule 51.513 was not at issue before the US Supreme Court, the Eighth Circuit did not reinstate Rule 51.513 on remand. Therefore, the only alternative left under the FCC rules is one that sets rates using a TELRIC cost model. There is no longer any applicable rule that permits the use of proxy rates for UNEs.

CenturyLink Ex. 4.0 at 7.

Staff avers that CenturyLink is essentially wrong, and while it is true that the actual proxy rates in Rule 51.513 were vacated by the Eighth Circuit, that fact is not relevant to Staff's position. In *Iowa Utilities Board v. FCC*, 219 F.3d 744 (8th Cir. 2000), Staff states the Appellate Court ruled that the FCC did not have authority to set specific proxy rates. The Court explained that:

The Supreme Court held that the FCC "has jurisdiction to design a pricing methodology." *AT & T Corp.*, 525 U.S. at 385. However, the FCC does not have jurisdiction to set the actual prices for the state commissions to use.

Setting specific prices goes beyond the FCC's authority to design a pricing methodology and intrudes on the states' right to set the actual rates pursuant to § 252(c)(2). Following the Supreme Court's opinion, we now agree with the FCC that its role is to resolve "general methodological issues," and it is the state commission's role to exercise its discretion in establishing rates.

*Iowa Utilities Board v. FCC*, 219 F.3d 744 at 757

Staff notes it is not proposing that the Commission use FCC proxy rates, rather Staff is proposing that the Commission set proxy rates that are just and reasonable, which is entirely consistent with the Iowa Utilities Board Court's conclusion.

Although the Eighth Circuit may have vacated the specific rates found in Sections 51.513, 51.611 and 51.707, Staff opines it expressly did not find unlawful the establishment and use of proxy rates by State Commissions. In fact, Staff notes the Commission may even use the specific vacated FCC proxy rates if arrived at independently, citing *Southwestern Bell Tel. Co. v. AT&T Comm.*, 1998 US Dist. LEXIS 15637, at 48-49, which stated that "[N]othing in the Eighth Circuit's decision prevents state commissions from independently concluding that the FCC's wholesale discount proxy rates are appropriate."

Moreover, Staff asserts the Eighth Circuit clearly reserved the right to set proxy rates to State Commissions, either in the manner the FCC set them or on the best evidence available, as long as they are just and reasonable, citing *Bell Atlantic-Delaware, Inc. v. McMahon*, 80 F. Supp. 2d 218 (Del. Dist. 2000) ("The Act allows the Commission to set rates based on the best evidence available to it [.]"); and Arbitration Decision, Hamilton Co., et. al., Petition for Arbitration with Verizon Wireless, ICC Docket Nos. 05-0644; 05-0645; 05-0646; 05-0647; 05-0648; 05-0649; 05-0657 (Cons.) (Jan. 25, 2006), 2006 Ill. PUC LEXIS 5, \*14-15 ("the Federal Act and the remaining FCC rules that were not vacated provide a basis for state commissions to establish default proxy rates within the discretion of the state commissions [.]").

As explained by Staff witness McClerren, Staff proposes as just and reasonable rates the 2-Wire Loop Rate at the proxy rate of \$17.93 and the CenturyLink proposed DS-1 Loop Rate of \$121.97.

Staff witness McClerren addressed whether or not the proposed prices developed by CenturyLink's TELRIC model appear just and reasonable, as required by Section 252(d)(1) of the 1996 Act. Table 1 shows the wholesale rates CenturyLink currently charges to NTS, CenturyLink's proposed wholesale rates, and NTS' proposed wholesale rates for the two disputed elements.

For the 2-Wire Loop, relative to CenturyLink's current rate, Staff notes that CenturyLink proposes a 50% rate increase, while NTS proposes a 30% rate decrease; while for the DS-1 Loop, again relative to CenturyLink's current rate, CenturyLink proposes a 33% rate decrease, while NTS proposes a 45% rate decrease.



Table 1

	Current CenturyLink Rate	Proposed CenturyLink Rate	Proposed NTS Rate
2-Wire Loop	\$17.93	\$26.85	\$12.50
DS-1 Loop	\$181.51	\$121.97	\$99.00

Mr. McClerren stated that it was his understanding that CenturyLink's current rates were the result of successful negotiations between CenturyLink's predecessor, Gallatin River Communications, and NTS, which concluded in August 2006, and were not based upon a TELRIC model. Mr. McClerren averred that Gallatin River Communications and NTS negotiated rates allowed a reasonable return for Gallatin River Communications. Further, Mr. McClerren indicated that he is unaware of strong upward or downward cost pressures relative to 2-Wire Loop or DS-1 Loop services since 2006.

Staff notes that Mr. McClerren disagreed with CenturyLink witness Ms. Londerholm who testified she concludes that CenturyLink's proposed UNE prices are reasonable when compared to Verizon Illinois' UNE pricing. Staff states that as shown in Table 2 below, Mr. McClerren considered Verizon Illinois' 21% lower rates for 2-Wire Loop and 15% lower rates for DS-1 Loop to be significantly lower than CenturyLink's proposed rates.

Table 2

	CenturyLink Monthly Rate	Verizon Monthly Rate	Percent Difference
2-Wire Loop	\$26.85	\$21.13	(21%)
DS-1 Loop	\$121.97	\$103.19	(15%)

Mr. McClerren indicated he had no reason to believe the Verizon Illinois rates were inadequate for Verizon Illinois to receive a reasonable return. Mr. McClerren focused on the comparability of Verizon Illinois' rates because he agreed with Ms. Londerholm, who testified that loop density (loops per square mile) is one of the largest factors affecting costs, and that Verizon Illinois' service area is the closest to CenturyLink's service area when comparing loop density. Mr. McClerren noted that, according to Ms. Londerholm, Verizon's Illinois service territory has a loop per square mile density of 28.1, while CenturyLink's Illinois service territory has a loop per square mile density of 48.1. Accordingly, Staff notes that CenturyLink's Illinois service territory has over 70% more loops per square mile than Verizon's Illinois service territory.

Mr. McClerren noted that a higher loop per square mile is significant because the higher the loop density per square mile, the shorter the average loop length will be, and the shorter the average loop length, the lower costs per loop. Accordingly, in Illinois, Staff asserts it would be reasonable to expect CenturyLink's proposed UNE prices to actually be lower than Verizon's UNE prices considering loop density; however Table 2 does not match that expectation.

Staff suggests that comparisons of different companies are complicated, and should only be used carefully, and would not, for example, advocate setting any rate based on a simple comparison of two companies. Staff states that differences between companies that could impact a comparison include geographical characteristics, regulatory differences, or economies of scale for purchasing. Regarding the validity of a Verizon and CenturyLink comparison, Mr. McClerren stated that the analysis is not obviously flawed, noting that regarding geographical characteristics, both companies are providing local exchange service in primarily suburban or rural Illinois, and most of their respective territories would require construction trenching through primarily soil-based rights-of-way, not rocky territory or through highly congested, concrete-covered sidewalks or streets likely found in urban areas. Staff states that considering regulatory differences, both companies are subject to the Commission's jurisdiction, so their regulatory requirements have been very similar. Regarding economies of scale for purchasing, historically, Staff avers that Verizon would have been able to acquire goods and services at relatively lower prices than CenturyLink due to Verizon's larger size, however, Staff notes CenturyLink acquired Qwest on April 1, 2011, making CenturyLink the third largest telecommunications carrier in the United States. On a going forward basis, Staff suggests CenturyLink should be able to acquire goods and services at discounted prices comparable to prices Verizon received.

Staff notes that Ms. Londerholm provides a comparison of CenturyLink properties in other jurisdictions as further support of rate reasonableness; however Staff states that her comparison is problematic and unpersuasive. Staff notes it does not provide the loop per square mile density numbers that Ms. Londerholm agrees represents one of the largest factors affecting an underlying carrier's cost.

Additionally, Mr. McClerren does not believe that the proposed rates developed by NTS witness Miri of 2-Wire Loop rates of \$12.50 and DS-1 Loop rates of \$99.00 are appropriate. Mr. McClerren notes that Mr. Miri utilized rates from AT&T Illinois as an approximation for NTS' proposed rates, however Staff questions the validity of comparing AT&T Illinois rates to CenturyLink rates given AT&T Illinois' loop per square mile metric of 465.9 compared to CenturyLink's loop per square mile metric of 48.1. While AT&T Illinois and CenturyLink are both regulated by this Commission, Staff notes that AT&T Illinois has operated under an alternative form of regulation since 1993, and is the only telecommunications carrier in Illinois to do so. Finally, Mr. McClerren notes that geographically, AT&T Illinois' service territory is primarily urban, which is very different than the suburban and rural nature of the CenturyLink territory.

Mr. McClerren states that there are four 2-Wire Loop rates possible in the record, and that any other rate advocated beyond those four rates would be arbitrary. Staff suggests the four possible 2-Wire Loop rates, in ascending order, are contained in Table 3.

Table 3

	NTS Proposed Rate	CenturyLink Current Rate	Verizon Rate	CenturyLink Proposed Rate
2-Wire Loop Rate	\$12.50	\$17.93	\$21.13	\$26.85

Staff notes Mr. McClerren does not support the NTS proposed 2-Wire Loop rate due to its reliance on AT&T Illinois' 2-Wire Loop rate as a foundation, while CenturyLink's proposed rate appears high, and is based upon CenturyLink's flawed TELRIC model. Staff suggests this effectively leaves the CenturyLink current 2-Wire Loop rate and the Verizon 2-Wire Loop rate as the remaining viable choices. Given that the CenturyLink current 2-Wire Loop rates are based on successful negotiations conducted by Gallatin River and NTS in 2006, that Staff is unaware of strong overall upward price pressure on 2-Wire Loops since 2006, and Verizon's 2-Wire Loop rates are based on a 70% lower loop per square mile density than CenturyLink's; Staff recommends that the Commission set the current CenturyLink 2-Wire Loop rate of \$17.93 as the just and reasonable 2-Wire Loop rate in this proceeding.

Regarding DS-1 Loop rates, Staff states there are 4 rates possible in the record, and argue that any other rate advocated beyond those four rates would be arbitrary. Staff notes that the four possible rates for DS-1 Loop rates, in ascending order, are contained in Table 4.

Table 4

	NTS Proposed Rate	Verizon Rate	CenturyLink Proposed Rate	CenturyLink Current Rate
DS-1 Loop Rate	\$99.00	\$103.19	\$121.97	\$181.51

Staff notes that Mr. McClerren does not support the NTS proposed DS-1 Loop rate due to its reliance on AT&T Illinois' DS-1 Loop rate as a foundation, while both CenturyLink and NTS propose rates below CenturyLink's current DS-1 Loop rate. Staff asserts this effectively leaves the Verizon DS-1 Loop rate and the CenturyLink proposed DS-1 Loop rate as the remaining viable choices.

Staff notes that Verizon's DS-1 Loop rate is based on a 70% lower loop per square mile density than CenturyLink's DS-1 Loop rate, therefore Staff suggests Verizon's DS-1 Loop rate should be higher than CenturyLink's DS-1 Loop rate. Staff opines that as Verizon's DS-1 Loop rate is close but actually lower than CenturyLink's

proposed DS-1 Loop rate, it would be reasonable to accept Verizon's DS-1 Loop rate as a reasonable proxy. Conversely, Staff notes that CenturyLink's proposed DS-1 Loop rate of \$121.97 is dramatically lower than the CenturyLink's current DS-1 Loop rate of \$181.51, a reduction of 33%. Staff states that NTS agreed in 2006's successful negotiations that CenturyLink's current DS-1 Loop rate of \$181.51 was acceptable. Staff believes that CenturyLink's proposed DS-1 Loop rate could also be found to be appropriate. Accordingly, both Verizon's DS-1 Loop rate of \$103.19 and CenturyLink's proposed DS-1 Loop rate of \$121.97 are defensible, and the Commission could select either and be within the parameters of just and reasonable. Nonetheless, Staff recommends that the Commission adopt the CenturyLink proposed DS-1 Loop rate because it is supported by a network model in the TELRIC study that is not flawed in the manner the network model is for the 2-Wire Loop rate.

Staff notes that Ms. Londerholm claims that Mr. McClerren's "just and reasonable" standard is inappropriate, arguing that he incorrectly applies a rate of return standard in testing the appearance of just and reasonableness, however Staff suggests Ms. Londerholm inappropriately conflates a "rate of return" standard with "just and reasonable" to reach the entirely unfounded conclusion that rate of return has no relevance in this proceeding. Staff asserts that Mr. McClerren clearly used the appropriate standard, the just and reasonable standard.

Staff opines that Mr. McClerren did not utilize a rate of return standard to establish whether or not the rates were just and reasonable, noting that Ms. Londerholm admitted on cross-examination that Mr. McClerren did not develop a revenue requirement, determine a rate base, proffer an allowed rate of return, or calculate operating expenses, depreciation, or taxes, all of which are required in a rate of return proceeding.

CenturyLink also complains that Mr. McClerren's loop density per square mile analysis is incomplete, claiming that higher loop density is not related to shorter loop length, and that other factors that drive increased cost include loop length and total area to be served. Staff notes that Ms. Londerholm speculates that, "In a square mile, CenturyLink's 48 customers could all be located out to the very edge from the central office while Verizon's 28 customers could be dispersed within close proximity of the central office," however Staff asserts that on cross-examination, Ms. Londerholm admitted that the converse could also be true, that you could just as easily flip the names Verizon and CenturyLink and the sentence would be true.

Staff suggests that Ms. Londerholm's customer dispersion analysis is entirely theoretical, and does not address the actual comparability of Verizon and CenturyLink service territories. Staff asserts that generically, exchanges are built in a "hub and spoke" design, with a central office near the geographical center of the largest town in an exchange. Staff states that both Verizon Illinois and CenturyLink provide local exchange service in primarily suburban or rural Illinois, and Ms. Londerholm admitted that she had done no dispersion comparison of Verizon and CenturyLink.

Staff opines that Ms. Londerholm testified that the prices proposed by CenturyLink were reasonable when compared to other Illinois ILECs, and then focused on Verizon as a fair test of reasonableness since Verizon Illinois' service area in Illinois is the closest to CenturyLink's service area when comparing the loop density. Staff asserts Ms. Londerholm's theoretical and flawed arguments in her rebuttal do not change the accuracy of her initial position about the appropriateness of comparing Verizon Illinois' and CenturyLink's UNE rates.

Staff states that Verizon Illinois' UNE rates do provide a valid comparison to CenturyLink UNE rates, and that comparison, when combined with the observations that CenturyLink current 2-Wire Loop rates are based on successful negotiations conducted by Gallatin River and NTS in 2006, that Mr. McClerren is unaware of strong overall upward price pressure on 2-Wire Loops since 2006, and that Verizon's 2-Wire Loop rates are based on a 70% lower loop per square mile density than CenturyLink's, indicate that the Commission should set the current CenturyLink 2-Wire Loop rate of \$17.93 as the just and reasonable 2-Wire Loop rate in this proceeding.

Staff notes that it supports the NTS legal conclusion that the Commission has the authority to set proxy rates in this proceeding.

While CenturyLink asserts that its cost model determines the most efficient network architecture, Staff disagrees. Staff explains that regarding two-wire loops, the network modeled by CenturyLink in its TELRIC study is capable of providing more services than CenturyLink's current network is capable of providing and, therefore, is inconsistent with the FCC's TELRIC prescriptions.

Staff notes that CenturyLink justifies its adoption of a 12,000-foot carrier service area ("CSA") based upon the fact that this design was adopted in other arbitrations, and that CenturyLink's primary argument is that the FCC had made a determination that a 12,000-foot breakpoint is required. Staff avers however, that the determination was made by the Common Carrier Bureau of the FCC acting in the stead of the Virginia State Corporation Commission. In particular, within its determination, the Wireline Competition Bureau stated:

In this proceeding, the Bureau, acting through authority expressly delegated by the Commission, stands in the stead of the Virginia State Corporation Commission (Virginia Commission) for the limited purpose of this arbitration.

Staff asserts the Seventh Circuit has addressed this very issue in deciding an analogous TELRIC methodology issue. In *MPower Communs. Corp. v. Ill. Bell Tel. Co.*, 457 F.3d 625, 631 (7th Circuit 2006), the Appellate Court explained that the District Court was wrong in stating that the FCC had "taken a stand" in the Virginia Arbitration Order on the issue of whether TELRIC demanded an assumption of 100% integrated digital loop carrier ("IDLC") equipment. Staff notes the Seventh Circuit explained that:

One problem with this conclusion is that□ ‘the FCC’ has not taken a stand. The Virginia dispute was arbitrated by the FCC’s Wireline Competition Bureau; that Bureau’s decision was not appealed to, or passed on, by the Commission. No one appointed by the President took any part in the proceedings. Under the Administrative Procedures Act, federal agencies make binding decisions through rulemaking or adjudication; the Virginia arbitration was neither. Statements by agencies’ bureaucracies (or their lawyers) may offer illumination helpful in understanding published rules or decisions. Here, however, there is no decision by the Commission in need of explication. All we have is action by subordinate employees.

*MPower Communs. Corp. v. Ill. Bell Tel. Co.*, 457 F.3d 625, 631 (7th Cir. 2006)(internal citations omitted)(“MPower”)

Thus, as the Seventh Circuit noted, it may certainly be informative to learn how the Wireline Competition Bureau interprets Federal statutes to make specific arbitration determinations, such determinations themselves, are in no way binding on the Commission. Staff agrees with CenturyLink that the Commission’s arbitration decisions must meet the requirements of Section 251 and the rules prescribed by the FCC pursuant to Section 251, however, Staff suggests a determination made by the Wireline Competition Bureau, acting in stead of the Virginia State Corporation Commission, in an arbitration involving different carriers in a different state in different market situations and with different network configurations are not binding on the Commission. A 12,000-foot breakpoint is neither required by Section 251 nor required by the FCC’s rules implementing Section 251. Staff states the Wireline Competition Bureau, not the FCC, was addressing an issue before it in an arbitration which had unique facts, and a 12,000-foot breakpoint may be appropriate and consistent with such statutes and rules under some circumstances, but certainly not in all circumstances and certainly not in the circumstances here.

Staff suggests the Seventh Circuit directly addressed this issue in the *MPower* case. In the underlying arbitration, Staff notes the Commission “concluded that an efficient provider would use about 88% universal digital loop carriers (“UDLCs”) and 12% IDLCs. Although IDLCs are less expensive per customer, they are also more difficult to use in providing UNEs to CLECs.” *MPower*, 457 F.3d at 631. The District Court, however, disagreed with the Commission’s conclusion based upon the Wireline Competition Bureau’s finding in the Virginia Arbitration case that used 100% IDLC. In upholding the ICC’s conclusion that 100% IDLC was not always the best mix for an efficient provider, the Seventh Circuit disagreed with the District Court explaining that:

A second problem is that, even if the Wireline Competition Bureau were speaking for the Commission, it did not establish a legal rule that 100% IDLC is the only setup that satisfies TELRIC. Both the Commission and the D.C. Circuit have stressed that there can be multiple ways to approximate that benchmark--which, since it is hypothetical and prospective, has no tried-and-true or mandatory elements. That’s what we

said three years ago. The Bureau used 100% IDLC in the Virginia proceeding, but to say (or demonstrate) that 'X is a lawful way to proceed' is not to establish that 'X is the only way to proceed.' Confusing sufficient with necessary conditions is a logical blunder. Nothing in the Virginia Arbitration Order implies that 100% IDLC is indispensable in all efforts to approximate a TELRIC price.

Id., at 631-32 (internal citations omitted).

Like the percentage of IDLCs used in TELRIC modeled network, Staff states there is nothing in the Virginia Arbitration Order that determines that a 12,000-foot breakpoint is the only way to proceed, and nothing in the Virginia Arbitration Order implies that a 12,000-foot breakpoint is indispensable in efforts to approximate a TELRIC price.

Staff notes that CenturyLink further cites an arbitration decision made by the Commission with respect to Illinois Bell Telephone as justification for its 12,000-foot breakpoint; however CenturyLink later argues that application of arbitrated rates that came from this arbitration are unreasonable because AT&T Illinois is not similarly situated to CenturyLink. Staff asserts that CenturyLink's argument that AT&T's territory is primarily urban and on average is about ten times as dense as CenturyLink's service territory, underscores the fact that arbitration determinations are not one size fits all. Staff avers that under CenturyLink's theory, the Commission would have no other option than to set rates based on a TELRIC model that is fatally flawed, which inherently means that the Commission would be setting unjust and unreasonable rates.

Staff also disagrees with CenturyLink's argument that the only attribute of the existing network that is to be included in a TELRIC cost is the location of the incumbent LEC's existing wire centers. Staff suggests the CenturyLink UNEs modeled should mirror the functionality contained in UNEs that CenturyLink is actually going to provide to any carrier that leases such UNEs. Without this constraint, Staff claims that the functionality included in the UNE that will be provided might bear no relationship to the UNE that is being modeled for cost purposes. Staff asserts that if the Commission were to accept CenturyLink's arguments, nothing would prevent a company from setting UNE costs based upon a network capable of providing ubiquitous broadband, video, or other services that cannot be provided using the capabilities contained in the actual UNEs being provided.

Staff notes this does not imply that CenturyLink must use the same technology or configuration contained in its current network; instead it must use the least cost technology and configuration necessary to provide the functionality that will actually be provided by CenturyLink. As the FCC has described its prescribed cost estimation methodology, "TRIC equates the current market value of the existing network of an incumbent telecommunications provider with the cost the incumbent LEC would incur today if it built a local network that could provide all the services its current network provides, to meet reasonably foreseeable demand, using the least-cost, most efficient technology currently available."

While CenturyLink also argues that adopting an 18,000-foot CSA design only marginally decreases the 2-wire loop UNE cost estimate in Band 1, Staff states that the fact that there is a lower cost technological configuration that allows CenturyLink to provide 2-wire loop UNEs with the functionality contained in CenturyLink's actual 2-wire loop UNE proves that CenturyLink's model is not based upon the least cost, most efficient technology currently available. While moving to an 18,000-foot CSA design yields only some reductions in cost, Staff asserts the 18,000-foot CSA is still a design that models ubiquitous broadband functionality and therefore more functionality than is in CenturyLink's current 2-wire loops. While, it is unclear to Staff how much greater the impact of modeling the actual functionality of CenturyLink's would be on cost reductions, the fact that CenturyLink has sought subsidies from the FCC for deployment of such a network suggests the difference is not insignificant.

For the reasons articulated by Staff and NTS, Staff recommends the Commission should find that the cost information submitted by CenturyLink is not an adequate basis upon which to set rates and reject CenturyLink's arguments to the contrary.

#### **D. Commission Analysis and Conclusion**

This is an interconnection arbitration conducted pursuant to Section 252 of the 1996 Act. CenturyLink has petitioned the Commission to arbitrate the rates for 2-wire and DS-1 unbundled loops to be purchased by NTS under the ICA that is to result from this proceeding. CenturyLink's proposed rates are the result of a TELRIC cost study that CenturyLink prepared. The Commission notes that both NTS and Staff take issue with certain aspects of CenturyLink's cost study and have proposed alternative rates that are based upon proxies that NTS and Staff contend the Commission can use to make its decision.

CenturyLink has proposed rates for unbundled 2-wire and DS-1 loops based on the TELRIC cost study, which yields suggested Band 1, 2 and 3 monthly recurring rates for 2-wire loops of \$26.85, \$52.83 and \$106.72, respectively, and for DS-1 loops of \$121.97, \$282.16 and \$618.79, respectively. It appears to the Commission that the two contested rates in this proceeding are the Band 1 2-wire, and the Band 1 DS-1 loop rates. NTS proposes that the Commission adopt proxy rates for CenturyLink and asserts that CenturyLink's Band 1 2-wire and DS-1 loop rates should be based upon AT&T's loop rates that were set in 2004 and that are applicable in Bartonville, Illinois. According to NTS, CenturyLink's Band 1 2-wire monthly recurring rate should be \$12.50 and its Band 1 DS-1 monthly recurring rate should be \$99. Staff also proposes proxy rates for the 2-wire loop rate. Staff proposes that the Commission should set a Band 1 2-wire monthly recurring rate of \$17.93, the rate set in a 2006 ICA negotiated by Gallatin River and NTS before CenturyLink acquired the Gallatin River exchanges in Illinois. The Commission notes that this rate was not based on a TELRIC cost study. Staff proposes that the Commission adopt CenturyLink's proposed Band 1 DS-1 monthly recurring rate.



Before discussing the specific proposals of the Parties, it is appropriate to first review the 1996 Act requirements and the FCC's rules concerning the pricing of UNEs. Section 251(c)(3) of the 1996 Act requires ILECs to provide nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms and conditions that are "just, reasonable and nondiscriminatory . . . ." 47 U.S.C. §251(c)(2). Section 252(d)(1)(A) of the 1996 Act in turn provides that the just and reasonable rate for network elements "(A) shall be (i) based on the cost (determined without reference to a rate-of-return or other rate based proceeding) of providing the interconnection or network element (whichever is applicable), and (ii) nondiscriminatory, and (B) may include a reasonable profit." 47 U.S.C. §252(d)(1).

In the FCC's initial regulations issued after passage of the 1996 Act, the FCC determined that an incumbent LEC's rates for UNEs such as 2-wire and DS-1 loops "shall be established, at the election of the state commission (1) Pursuant to the forward-looking economic cost-based pricing methodology set forth in §§51.505 and 51.511; or (2) Consistent with the proxy ceilings and ranges set forth in §51.513." 47 C.F.R. §51.503(b). Section 51.505 of the FCC's rules provides that "[t]he forward-looking economic cost of an element equals the sum of: (1) The total element long-run incremental cost of an element, as described in paragraph (b); and (2) A reasonable allocation of forward-looking common costs, as described in paragraph (c)." 47 C.F.R. §51.505. Section 51.513 of the FCC's rules was appealed and later vacated by the Eighth Circuit in *Iowa Utilities Board v. FCC*, 219 F.3d 744 (8th Cir. 2000), rev'd in part on other grounds, *Verizon Communications, Inc. v. FCC*, 535 U.S. 467 (2002).

CenturyLink asserts that the FCC's existing regulations only authorize a state commission to set UNE rates based on the FCC's forward-looking economic cost-based pricing methodology. NTS and Staff however argue that the Commission still retains the authority to set prices using a proxy rate, based on the best evidence available, as long as they are just and reasonable.

"Total element long run incremental cost" is a term that goes by the acronym "TELRIC." Under the FCC's rules, the TELRIC of an element is the forward-looking cost over the long run of the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such an element. 47 C.F.R. §51.505(b). TELRIC is measured based on the use of the most efficient telecommunications technology currently available and the lowest cost network configuration, given the existing location of the incumbent LEC's wire centers. 47 C.F.R. §51.505(b)(1). The FCC's rules also require that TELRIC be calculated using a forward-looking cost of capital and economic depreciation rates. 47 C.F.R. §51.505(b)(2)&(3).

In this case, CenturyLink presented a TELRIC cost study which it suggests support the rates it proposes in this arbitration proceeding. To develop the TELRIC component of the forward-looking economic cost of 2-wire and DS-1 loops, CenturyLink asserts its cost model determined the forward-looking, most efficient network architecture and calculated the forward-looking installed cost of UNE loops based on this architecture. The combined use of existing wire center locations and boundaries,

geo-coded customer locations, actual road networks and terrain features purportedly allows CenturyLink's TELRIC model to design, engineer and construct the most efficient cable routes possible relative to these inputs and parameters. In addition, equipment items (e.g. Digital Loop Carriers, Cross Connects, Cables and Terminals) are designed and sized to a capacity to achieve efficiency to meet the total demand for services at the locations served by the equipment. In this way, CenturyLink's cost model is intended to satisfy the requirement that TELRIC be based upon the most efficient telecommunications technology currently available and the least cost network configuration given the existing locations of CenturyLink's wire centers.

Once the forward-looking installed cost is calculated, CenturyLink's cost model calculates capital and expense costs. The Direct Costs attributable to UNE loops consist of maintenance expenses and other direct network operations and support expenses. Maintenance costs include such things as repairing damaged cable or maintaining digital circuit equipment. Other direct network operations and support expenses include such things as testing functions, circuit engineering and cable pair record maintenance. CenturyLink argues that in accordance with the FCC regulations, its TELRIC cost model uses a forward-looking cost of capital and forward-looking depreciation rates.

CenturyLink suggests the rates calculated by its TELRIC cost study also include a reasonable allocation of forward-looking common costs. Common costs include such costs as accounting and information technology personnel, furniture, office equipment, general purpose computers and corporate operations. CenturyLink's cost study calculates a common cost factor using the current common costs in Illinois and dividing by Illinois TELRIC annual expenses. This factor is then applied back to the individual TELRIC annual expenses to allow for recovery of common costs in the monthly recurring 2-wire and DS-1 loop rates.

The Commission notes that both NTS and Staff criticize certain aspects of CenturyLink's cost study. In its testimony, NTS for the most part merely questioned the inputs to CenturyLink's cost study; however it does not appear that NTS proposed alternative inputs to be used in the cost study to produce alternative rates during the course of negotiations or in its testimony. NTS witness Miri opined that the annual charge factors in the cost study are higher than he has seen in other cost studies; however, he did not state that they were incorrect for CenturyLink's rural service territory. It does not appear to the Commission that either NTS or Staff disputed that costs are higher in rural exchanges because rural exchanges have lower line densities than urban or suburban exchanges.

Staff challenges the TELRIC cost study, contending that it is not appropriate for the cost study to be based on a network design that uses a 12,000 foot breakpoint between copper and fiber. According to Staff, the 12,000 foot breakpoint and the DLCs at the copper/fiber breakpoint make the network modeled in CenturyLink's cost study capable of providing more services than CenturyLink's current network is capable of providing. Specifically, Staff asserts that the 12,000 foot breakpoint makes the loops in the modeled network ubiquitously capable of providing broadband.

CenturyLink suggests that the FCC has addressed the use of the 12,000 foot breakpoint between copper and fiber and has held that it is the proper design to be used in a TELRIC cost study. *In the Matter of the Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc., and for Expedited Arbitration In the Matter of Petition of AT&T Communications of Virginia, Inc., Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia Corporation Commission Regarding Interconnection Disputes with Verizon Virginia, Inc.*, 18 FCC Rcd 17722, ¶241 (Rel. August 29, 2003). CenturyLink argues the FCC's determination on this point is binding on the Commission, just as it was upon CenturyLink for model criteria use. CenturyLink notes the Commission has approved the use of this design in the two prior UNE proceedings in Illinois. *Illinois Bell Telephone Company Filing to Increase Unbundled Loop and Nonrecurring Rates*, Docket 02-0864, 2004 Ill. PUC LEXIS 339, \*263, 298-99 (Illinois Commerce Commission June 9, 2004); *Verizon North Inc. (f/k/a GTE North Incorporated) and Verizon South Inc. (f/k/a GTE South Incorporated), Petition Seeking Approval of Cost Studies for Unbundled Elements, Avoided Costs and Intrastate Switched Access Services*, Docket No. 00-0812.

Staff bases its argument that it is not appropriate to use a 12,000 foot copper/fiber breakpoint on the FCC's *Triennial Review Order*. Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, *In the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket Nos. 01-338, 96-98 and 98-147, 18 FCC Rcd 16978 (Rel. Aug. 21, 2003) ("Triennial Review Order"), vacated in part on other grounds *United States Telecom Association v. FCC*, 359 F.3d 554 (D.C. Cir. 2004). Staff cites paragraph 669 of the Triennial Review Order in which the FCC stated that "TELRIC equates the current market value of the existing network of an incumbent telecommunications provider with the cost the incumbent LEC would incur today if it built a local network that could provide all the services its current network provides, to meet reasonably foreseeable demand, using the least-cost, most-efficient technology currently available." Staff contends that the under-lined language means that the network modeled in a TELRIC cost study cannot be capable of providing more or different services than the existing network provides.

Staff argues the network modeled by CenturyLink in its TELRIC study is capable of providing more services than CenturyLink's current network is capable of providing and, therefore, is inconsistent with the FCC's TELRIC prescriptions. Staff opines that CenturyLink has modeled a network with the ubiquitous capability to provide higher bandwidth or broadband services, however, Staff notes CenturyLink's actual network does not contain such ubiquitous capability.

CenturyLink argues that Staff's reliance upon the italicized language from the Triennial Review Order is misplaced, and the italicized phrase that Staff relies upon

prescribes a minimum, not a maximum. CenturyLink contends the network modeled in a TELRIC study must be capable at a minimum of providing all of the services that the existing network provides, and the italicized phrase in no way prohibits the modeled network from being capable of providing more services than the existing network provides.

As the TELRIC cost study has modeled capabilities beyond what the existing network provides, Staff suggests the Commission should reject that portion of the cost study, and set proxy rates. Staff asserts the Eighth Circuit clearly reserved the right to set proxy rates to State Commissions, either in the manner the FCC set them or on the best evidence available, as long as they are just and reasonable, citing *Bell Atlantic-Delaware, Inc. v. McMahon*, 80 F. Supp. 2d 218 (Del. Dist. 2000) (“The Act allows the Commission to set rates based on the best evidence available to it [.]”); and Arbitration Decision, Hamilton Co., et. al., Petition for Arbitration with Verizon Wireless, ICC Docket Nos. 05-0644; 05-0645; 05-0646; 05-0647; 05-0648; 05-0649; 05-0657 (Cons.) (Jan. 25, 2006), 2006 Ill. PUC LEXIS 5, \*14-15 (“the Federal Act and the remaining FCC rules that were not vacated provide a basis for state commissions to establish default proxy rates within the discretion of the state commissions [.]”).

The Commission agrees with Staff and NTS that the Commission retains the authority to set proxy rates should the Commission not be presented with an appropriate TELRIC study.

In addition to questioning various inputs to CenturyLink's cost study, NTS also pointed out that a small portion of CenturyLink's airplane costs are included in the cost study. CenturyLink argues that NTS did not dispute that the cost of airplanes is an example of a common cost that is properly allocated to unbundled loops under the FCC's rules. NTS also asserted that retail costs are included in the cost study. However, CenturyLink suggests its cost study removed all retail related expenses in calculating the TELRIC cost for 2-wire and DS 1 loops. NTS also questioned how the cost study handled poles owned by electric utilities. CenturyLink asserts that it demonstrated that the cost study properly handled pole costs, by reducing investment in poles to account for poles owned by electric utilities.

The Commission finds that CenturyLink's TELRIC cost study as filed is not appropriate for setting the 2-wire loop rates in this proceeding, and agrees with Staff that since there is a lower cost technological configuration that allows CenturyLink to provide 2-wire loop UNEs with the functionality contained in CenturyLink's actual 2-wire loop UNE, CenturyLink's model is not based upon the least-cost, most efficient technology currently available. The Commission finds that CenturyLink's cost study does not comply with the FCC's TELRIC cost study rules and produces rates for 2-wire loop UNEs that are not just, reasonable and nondiscriminatory. The criticisms levied by Staff to the TELRIC cost study, however, appear only to be in relation to the calculation of the DS-1 loops.

CenturyLink suggests that should the Commission accept Staff's criticism of the 12,000 foot copper/fiber breakpoint design, it would amount to only a minor and easily

changed input in the cost study and the Commission is authorized under federal law to order specific and supportable input changes in its determination. In its testimony, CenturyLink claims it quantified the effect of moving to an 18,000 foot breakpoint design amounted to less than \$1 per loop in Zone 1. CenturyLink suggests it also quantified the effect of removing what Staff considered to be an excessive number of DLCs from the cost study and that effect was also very small.

The Commission agrees with CenturyLink that NTS' criticisms of the TELRIC cost study do not require changes to the study. The Commission believes that CenturyLink has adequately addressed these issues. The Commission does find however that Staff's criticisms are well-founded, and that these changes should be adopted for the TELRIC cost study to be used for setting just and reasonable rates in this proceeding. The Commission agrees with CenturyLink that the Commission is authorized to order specific and supportable input changes in its determination. As CenturyLink indicates in its testimony that it has already modeled both changes, the Commission finds that the appropriate Loop 1 2-wire rate to be adopted by the parties in this proceeding should be the rate developed by running the TELRIC cost model with the changes suggested by Staff. While CenturyLink claims that each suggested change is minor and inconsequential, it appears to the Commission that the total of the changes could be more than minor and inconsequential, and it would not be appropriate to set rates in this proceeding without accounting for those suggested changes. The Commission therefore directs CenturyLink to perform a new TELRIC cost study based on the evidence presented in this proceeding, modeling the changes to the inputs recommended by Staff, and that the resulting rates developed by the TELRIC cost study for the Band 1 2-wire loop rate shall be adopted for the purposes of this arbitration. The Commission will also address the proxy rates suggested by NTS and Staff, although they will not be adopted for this proceeding.

The Commission agrees with Staff and CenturyLink that NTS' suggested proxy is inappropriate as a proxy as it relies on AT&T Illinois' 2-wire loop rate as a foundation. The Commission notes that the rates proposed by NTS for Band 1 2-wire and DS-1 loops are based on UNE rates prescribed for AT&T over eight years ago, which rates have not been updated to reflect today's costs. The Commission also recognizes that AT&T's service territory is predominantly urban and more dense than CenturyLink's service territory in Illinois. Consequently, even if the rates had been updated, AT&T rates would not be appropriate proxies for what a TELRIC cost study would produce for CenturyLink's rural service territory. Accordingly, the Commission declines to adopt the proxy proposals presented by NTS.

Staff proposes as just and reasonable rates the 2-wire Loop Rate currently in use, which is based on successful negotiations between Gallatin River and NTS in 2006, noting that it does not appear that there is strong upward price pressure on 2-wire loops since 2006. The Commission finds that it is not necessary to adopt the rate proposed by Staff for the Band 1 2-wire loop, as appropriate changes are able to be made to the TELRIC cost study, adopting Staff's criticisms, to develop a just and reasonable rate for Band 1 2-wire loops.

Staff notes that Verizon's DS-1 Loop rate of \$103.19 is based on a 70% lower loop per square mile density than CenturyLink's DS-1 Loop rate, suggesting that Verizon's DS-1 Loop rate should be higher than CenturyLink's DS-1 Loop rate. The Commission notes that Verizon's DS-1 Loop rate is close to, but actually lower than CenturyLink's proposed DS-1 Loop rate, and that Staff therefore suggests it would be reasonable to accept Verizon's DS-1 Loop rate as a valid proxy. The Commission also recognizes that CenturyLink's proposed DS-1 Loop rate of \$121.97 is dramatically lower than CenturyLink's current DS-1 Loop rate of \$181.51. The Commission notes that NTS agreed in negotiations in a prior docket that CenturyLink's current DS-1 Loop rate of \$181.51 was acceptable. Staff believes that CenturyLink's proposed DS-1 Loop rate could also be found to be appropriate, therefore Staff suggests that both Verizon's DS-1 Loop rate of \$103.19 and CenturyLink's proposed DS-1 Loop rate of \$121.97 are defensible, and the Commission could select either and be within the parameters of just and reasonable. Nonetheless, Staff recommends that the Commission adopt the CenturyLink proposed DS-1 Loop rate because it is supported by a network model in the TELRIC study that is not flawed in the manner the network model is for the 2-Wire Loop rate. The Commission agrees with Staff and CenturyLink that the DS-1 rate from the TELRIC study is an appropriate rate. The Commission recognizes that the flaws present in the 2-wire loop portion of the TELRIC cost study are not present for the DS-1 portion of the cost study; therefore, the Commission will accept the rate developed by this portion of the TELRIC cost study.

## **V. ARBITRATION STANDARDS**

Under Section 252(c) of the Federal Act, the Commission is required to resolve open issues, and impose conditions upon the parties, in a manner that comports with three standards. The Commission holds that the analysis in this arbitration decision satisfies that requirement.

First, Section 252(c)(1) directs the state commissions to "ensure that such resolution and conditions meet the requirements of section 251, including the regulations prescribed by the [FCC] pursuant to section 251." In this arbitration, the Commission has directed the parties to include provisions in their ICA that fully comport with Section 251 requirements and FCC regulations.

Second, Section 252(c)(2) requires that the Commission "establish any rates for interconnection, services or network elements according to subsection [252(d)]." Here, most of the pertinent rates were already established by the parties through mutual agreement. Insofar as the Commission's resolution of open issues will affect those or other rates in the parties' ICA, the Commission requires, and expects the parties to establish, rates that are in accord with Section 252(d) of the Federal Act.

Third, pursuant to Section 252(c)(3), the Commission must "provide a schedule for implementation of the terms and conditions by the parties to the agreement." Therefore, the Commission directs that the parties file, within 14 calendar days of the date of service of this arbitration decision, their complete ICA for Commission approval pursuant to Section 252(e) of the Federal Act.

Fourth, the Commission disposes of all motions, petitions, objections, and other matters in this proceeding which remain unresolved in a manner consistent with the conclusions herein.

DATED: June 14, 2012

Briefs on Exceptions to be filed by June 21, 2012

Reply Briefs on Exceptions to be filed by June 28, 2012

J. Stephen Yoder  
Administrative Law Judge